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April 23, 2009

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BY HAND

The Honorable Anne K. Quinlan, Esq.
Acting Secretary
Surface Transportation Board
395 E Street, SW
Washington, D.C. 20423-0001

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Re: STB Ex Parte 431 (Sub-No.3)
Review of Surface Transportation Board's General Costing System

Dear Secretary Quinlan:

Enclosed for filing in the above-referenced proceeding are an original and ten copies of the Written Submission of Arkansas Electric Cooperative Corporation.

If you have any questions or I can be of any assistance, please let me know.

Respectfully,



George W. Mayo, Jr.

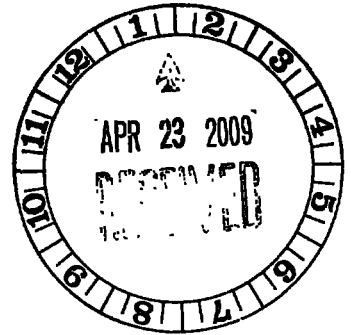
Enclosures

BEFORE THE
SURFACE TRANSPORTATION BOARD

EX PARTE NO. 431 (Sub-No. 3)

REVIEW OF THE SURFACE TRANSPORTATION BOARD'S
GENERAL COSTING SYSTEM

WRITTEN SUBMISSION OF
ARKANSAS ELECTRIC COOPERATIVE CORPORATION



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Pursuant to the Board's notice dated April 6, 2009, this document provides the notice of intent to participate and written comments of Arkansas Electric Cooperative Corporation (AECC) regarding the public hearing scheduled for April 30, 2009 to examine issues related to the Uniform Railroad Costing System (URCS), and the Board's determination whether and to what extent modifications to URCS are needed.

I. NOTICE OF INTENT

At the public hearing, AECC's views will be presented by Steve Sharp. Mr. Sharp is the Principal Engineer – Fuels & Civil for AECC. AECC requests that the Board allow 10 minutes for Mr. Sharp's comments, which will focus on the efficiency adjustments associated with unit-train movements, the costing of TOFC/COFC traffic, the statistical relationships used in URCS (including the variability estimates), and private car costs.

II. STATEMENT OF INTEREST

AECC is a membership-based generation and transmission cooperative that provides wholesale electric power to electric cooperatives, which in turn serve approximately 490,000 customers located in each of the 75 counties in Arkansas. In

order to serve its member distribution cooperatives, AECC has entered into arrangements with other utilities within the state to share generation and transmission facilities. The largest of AECC's generation assets are its ownership interests in the White Bluff plant at Redfield, AR and the Independence plant at Newark, AR, each of which typically burns in excess of 6 million tons of Powder River Basin (PRB) coal annually. AECC holds a 35 percent interest in each of these plants (for which Entergy is the operator and majority owner). In addition, AECC holds a 50 percent interest (with American Electric Power) in the Flint Creek plant, which is located at Gentry, AR. This plant normally burns in excess of 2 million tons of PRB coal annually.

As a result of the large volume of PRB coal used by these plants and the essential role of rail transportation for these movements, AECC has a direct interest in actions by the Board that affect its rail transportation options. As described in further detail in comments recently submitted by AECC in Ex Parte No. 681,¹ AECC's specific interest in URCS refinements stems from the role of URCS determinations of variable costs in coal rate reasonableness cases. The Independence and Flint Creek plants are each served exclusively by a single rail carrier, and prospectively may need to rely on Board rate reasonableness procedures to constrain the exercise of rail market power.

¹ STB Ex Parte No. 681, Class I Railroad Accounting and Financial Reporting - Transportation of Hazardous Materials, "Comments of Arkansas Electric Cooperative Corporation on Proposed Rule-Making" (February 4, 2009) (hereafter, "AECC URCS/Hazmat Comments") at pages 4-5.

III. COMMENTS

AECC's comments fall into four of the categories specified in the Board's April 6 notice,² addressing whether and how the Board could:

1. Improve the efficiency adjustments associated with unit-train and multi-car movements;

3. Improve the costing of trailer or container on flat car (TOFC/COFC) traffic;

6. Disaggregate loss and damage information by carrier and by two-digit Standard Transportation Commodity Code (STCC) groupings; and,

13. Update the various statistical relationships used in URCS, including the variability estimates.

In addition, AECC suggests that the Board revisit the URCS treatment of private car costs it adopted in 1997. Each of these issues is addressed below.

AECC's comments are based on descriptions provided by the Board and other credible sources regarding URCS logic and methods. Available documentation regarding the actual contents of "Phases I and II" of URCS appears to be quite scarce. While the Board's website provides free copies of the URCS "Phase III" movement costing model, AECC's search of the Board's website, other rail transportation research resources, and the internet suggests that documentation of the analyses that form the foundation of URCS is, at best, hard to find. Moreover, it is often in the nature of computer programs and regression analyses that the actual computations embody assumptions, methods, and data that are not explicitly stated in the documentation. In the 17 days since the Board's

² AECC's comments stem from the relevance of these categories to the costing of unit coal train movements. In presenting comments in only these categories, AECC does not assert or imply that refinements in other categories or related to other topics may not also be warranted.

notice of this proceeding was published, AECC has not replicated or validated the computer code or the documentation associated with the URCS analyses. Board efforts to improve URCS should provide adequate opportunities for participants to perform such replication and validation, thereby improving the transparency of current procedures and proper implementation of conceptual reforms that the Board may choose to pursue.

Issue # 1: Efficiency Adjustments Associated With Unit-Train Movements

Since the time URCS was originally developed, the proliferation of increasingly efficient unit-trains has been a consistent feature of U.S. rail operations. PRB coal users like AECC have had an active role in this process, investing in high-capacity cars and unloading facilities that have supported the operation of longer unit-trains with greater payloads. Outside of coal, similar trends can be seen in a wide range of commodity flows, from double-stack intermodal trains, to grain shuttle trains, to the development of unit trains for ethanol distribution. Unit-train operations are able to achieve a much higher level of efficiency compared to the traditional individual handling of cars in way/through train operations, which is the principal reason why use of this type of rail operation has increased so dramatically.

As described by the Board, URCS reflects the efficiencies of unit-train operations through “5...adjustments that are applied to trainload (50 car or more) movements:

(1) origin and destination switching are reduced by 75%; (2) interchange costs are reduced by 50%; (3) inter- and intra-train switching costs are eliminated; (4) no way train costs are used; and (5) station clerical costs are reduced by 25% for each car.”³ While

³ See STB Ex Parte No. 431 (Sub-No. 2), Review of the General Purpose Costing System, decision served October 1, 1997 at page 4, fn 15. Based on the description of URCS refinements presented in this

these adjustments are not insignificant, they appear to be ad hoc, and do not ensure that URCS accurately reflects the efficiencies relative to system average single-car costs now achievable on unit-train movements.

Nowhere are such efficiencies more apparent than on long-distance unit coal train movements originating in the PRB. Trains containing up to 150 light-weight cars move up to 18,000 net tons at once, frequently using only 4 locomotives and a single 2-person crew. Moreover, as described in a fuel-use study submitted by AECC to the Board,⁴ a large portion of PRB coal moves in the corridor toward Kansas City, where favorable topography further enhances the efficiency of operations.

Highly efficient PRB movements constitute a significant portion of the total universe of U.S. rail traffic. In 2007, DOE/EIA reports that coal originating in the Wyoming portion of the PRB alone accounted for 436.5 million tons,⁵ which corresponds to over 20 percent of the Class I total originations of 1.940 billion tons reported by AAR. At an average length of haul of 1000 miles or more, Wyoming PRB coal alone represents close to 25 percent of all reported net rail ton-miles in the U.S.

With this much traffic moving this efficiently, the Board must take care to ensure the validity of URCS costs. For example, use of 25% of system average origin and destination switching might have been reasonable in an environment where a train was made up of cuts of cars from different mines and/or had to be broken down for unloading.

document, it is understood that these volume movement adjustments date back to the original implementation of URCS in 1989.

⁴ See pages 6-8 and Table 2 in "Rail Fuel Use and Surcharges for White Bluff and Independence Plants", submitted to the Board May 15, 2006 pursuant to a request made by Chairman Buttrey at the public hearing held on May 11, 2005 in Ex Parte No. 661, Rail Fuel Surcharges.

⁵ See <http://www.eia.doe.gov/cneaf/coal/page/acr/table2a.html> .

However, for most PRB coal trains, origin and destination switching certainly appears to be less than 25% of the system average. Unit-trains cycle intact through mine loop tracks for loading, and PRB coal users like AECC run unit-trains intact through their own loop track unloading facilities. On customer-provided unit-trains like AECC's, no car switching is normally needed at origin or destination. Under these circumstances, the URCS unit-train adjustment – which dates from the original implementation of URCS in 1989 - doesn't reflect the actual savings associated with current operations.

Similarly, if unit-train interchange costs are less than 50 percent of the system average – as indicated by the Board in its approval of the UP/SP merger⁶ - the unit-train adjustment doesn't reflect the actual interchange cost savings. Likewise, if station clerical costs are reduced by more than 25% per car, the unit-train adjustment fails to capture the actual savings.

In each instance where the unit-train adjustment fails to reflect actual savings, coal shippers are subject to being overcharged by an amount equal to 180 percent of the error (i.e., due to application of the jurisdictional threshold to erroneously high variable costs). Such occurrences violate the Board's mandates under 49 U.S.C. § 10101 (2) to provide fair regulatory decisions, under 49 U.S.C. § 10101 (5) to foster sound economic conditions in transportation, under 49 U.S.C. § 10101 (6) to maintain reasonable rates where there is an absence of effective competition, and especially under 49 U.S.C.

⁶ See STB Finance Docket No. 32760, Union Pacific Corporation, Union Pacific Railroad Company, And Missouri Pacific Railroad Company--Control and Merger—Southern Pacific Rail Corporation, Southern Pacific Transportation Company, St. Louis Southwestern Railway Company, SPCSL Corp., and The Denver and Rio Grande Western Railroad Company, Decision No. 44 (August 6, 1996) at page 154, where the Board stated that “(i)nterline movements do not significantly detract from the efficiencies of run-through coal unit trains.”

§ 10101 (13) to ensure the availability of accurate cost information in regulatory proceedings.

To avoid such outcomes, the Board should initiate a proceeding or perform a special study that more reliably quantifies the unique cost characteristics of the most efficient unit-train movements, including PRB coal. Alternatively, or as an interim measure, the Board should create one or more new categories of unit-train adjustments that reflect actual levels of efficiency now achieved by different unit-train and multiple-car movements.

Issue # 3: Costing of TOFC/COFC Traffic

TOFC/COFC is similar to PRB coal traffic in that it has grown dramatically since the introduction of URCS (to a typical annual volume on the order of 12 million units) and achieves efficiencies through trainload movements. However, its cost characteristics differ dramatically from those of PRB coal in ways that currently are not reflected by URCS.

As discussed in AECC's comments in Ex Parte No. 681, TOFC/COFC tends to be highly fuel-intensive.⁷ In the absence of appropriate adjustments, use of system average data will cause other commodities to cross-subsidize the fuel consumption of intermodal.

In addition, while the high average speed of intermodal trains holds down direct crew and locomotive hours for any given length of haul, the high dispatch priority such trains enjoy tends to increase the incurrence of such costs in movements of other traffic. Intermodal also incurs capital and operating costs associated with dedicated facilities and activities.

⁷ AECC URCS/Hazmat Comments at pages 6-7.

The Christensen study released in 2008 by the Board acknowledged that the cost characteristics of the growing intermodal segment may be different from the system average to a degree that would create the artificial impression of a productivity decrease.⁸ URCS requires modification sufficient to ensure that growth in the high-cost intermodal segment does not apply artificial upward pressure on “system average” costs that improperly affects URCS results for other commodities. As is the case with the most efficient unit-train traffic, intermodal traffic warrants attention in a proceeding or special study to ensure that its costs are properly recognized by URCS.

Item # 6: Disaggregate Loss and Damage Information

The Board’s proposal to disaggregate loss and damage information by commodity group and carrier is intrinsically meritorious as a method for promoting accountability and responsibility. For example, shippers of low-value commodities, including coal, should not be paying loss and damage costs for containers of imported electronics damaged in transit by slack action, etc., or stolen from a spot in an intermodal yard.

Item # 13: Update Statistical Relationships in URCS

The core of URCS is formed by a series of econometric analyses of costs drawn from rail accounting data. While a detailed assessment of model specification and other econometric issues for individual URCS regressions is beyond the scope of these comments, scholarly reviews of such issues have been conducted that make clear the need for a thorough review of the URCS models. For example, a study sponsored by FRA highlighted issues associated with the lack of theoretical foundation, the potential

⁸ See Laurits R. Christensen Associates Inc., A Study of Competition in the U.S. Freight Railroad Industry and Analysis of Proposals That Might Enhance Competition, Volume 2, Analysis Of Competition, Capacity, And Service Quality, pages 9-16 to 9-18.

bias in results introduced by the absence of intercept terms, the failure to reflect known economies of density and opportunities for substitution among input factors, violations of the underlying assumptions of the ordinary-least-squares (OLS) estimator used, and various other apparent faults.⁹ The same study illustrated an opportunity that apparently exists to improve the rigor of the cost estimates for different traffic types by including separate output measures in the model (so-called “hedonic” cost models).

The Board should therefore pursue substantial refinements of the URCS model system to address its identifiable shortcomings. Such refinements should include, but by no means be limited to, specification changes that add intercept terms, reflect economies of density and input substitutability, and provide separate volume measures for major traffic groups whose costs differ materially from system averages (PRB coal, other unit train, TOFC/COFC, etc.).

Additional Item: Private Car Costs

In its limited review of URCS issues conducted in 1997, the Board initially indicated that “...we will tentatively modify our costing procedures to assume that all privately owned car types that show no mileage allowance in the CHARMS file incur no car cost, except for railroad-owned pool cars (for which an allowance is always paid).”¹⁰ This appeared to implement the fundamental principle that the railroads should not count as costs items for which they do not pay (directly or indirectly). However, after AAR argued that in some cases the CHARMS file erroneously shows zero car cost where

⁹ See Wilson, W. and J. Bitzan, “Costing Individual Railroad Movements”, prepared for Federal Railroad Administration (September 2003) at pages 9-11.

¹⁰ See STB Ex Parte No. 431 (Sub-No. 2), Review of the General Purpose-Costing System, decision served October 1, 1997 at page 8.

critical data elements are unreported, the Board decided¹¹ that “(w)e will instead use, as suggested by AAR, the mileage rates developed from the R-1 Annual Report currently used in URCS movement costing.”

Whatever may be the shortcomings of CHARMS, the fact is that this decision means coal users like AECC get charged a mileage rate by URCS for the cars we supply, even though we bear the entire cost of car supply – at no charge to the railroad - for the large dedicated fleet needed to move our coal. The Board should correct this error, and ensure that URCS properly removes from the cost computation all costs that are borne by parties other than the rail carrier(s).

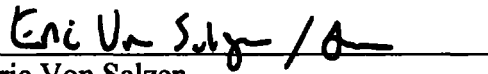
AECC appreciates this opportunity to participate in the Board’s consideration of potential URCS refinements.

Respectfully submitted,

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¹¹ See STB Ex Parte No. 431 (Sub-No. 2), Review of the General Purpose Costing System, decision served December 12, 1997 at page 4.